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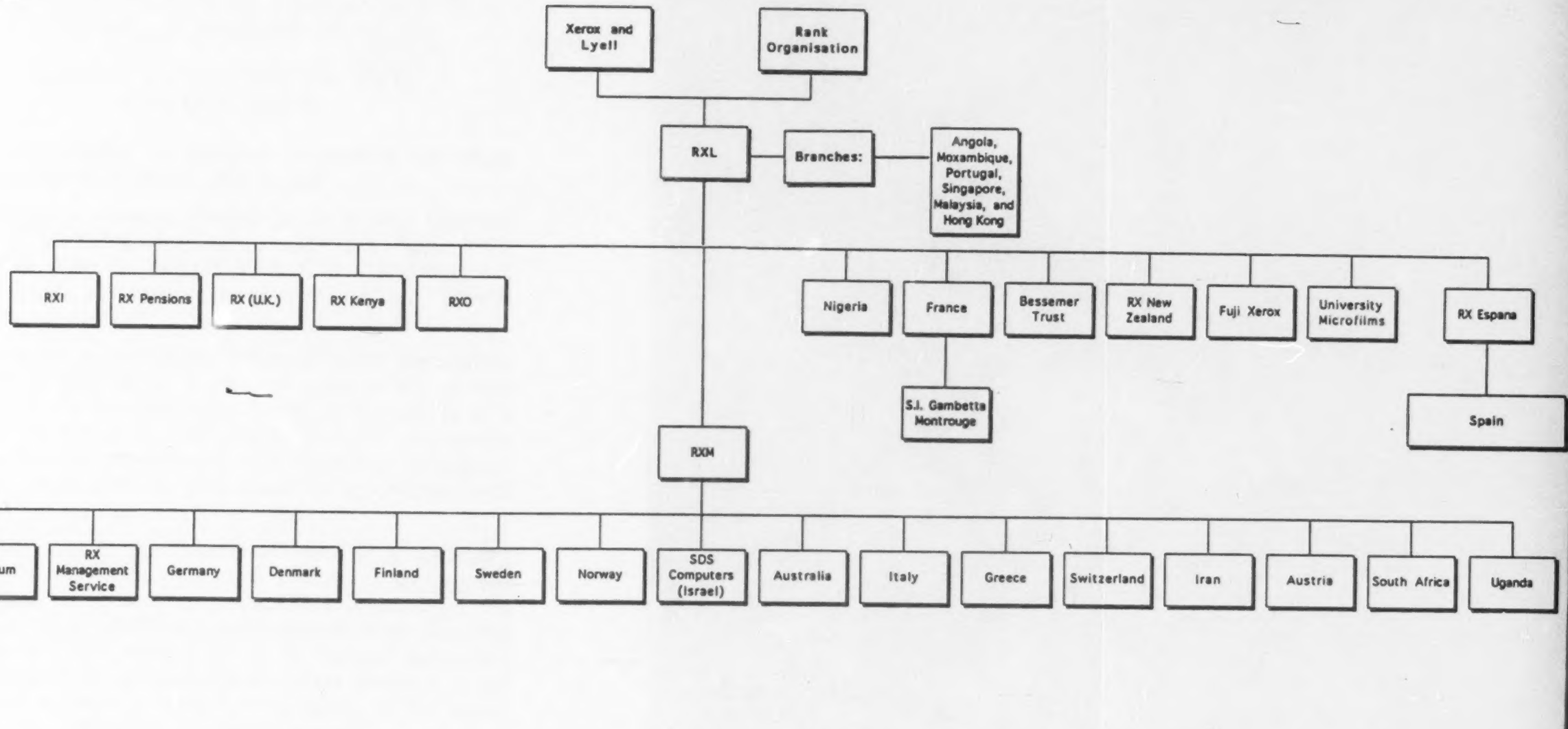
APPENDIX A

[Corporate Structure of Rank-Xerox, Ltd. and its Subsidiaries]



APPENDIX B

[U.K. Finance Act of 1972, Sections 84, 85, 86 & 92]

PART V—TAXATION OF COMPANIES AND COMPANY DISTRIBUTIONS

ADVANCE CORPORATION TAX AND TAX CREDIT

SEC. 84 Liability for advance corporation tax where company makes qualifying distribution

84(1) Where a company resident in the United Kingdom makes a qualifying distribution after 5th April 1973 it shall be liable to pay an amount of corporation tax (to be known as "advance corporation tax") in accordance with this section.

84(2) Subject to section 89 below, advance corporation tax shall be payable on an amount equal to the amount or value of the distribution, and shall be so payable at a rate (to be known as "the rate of advance corporation tax") which for the financial year 1986 and subsequent financial years shall be determined in accordance with section 17 of the Finance Act of 1986.

84(3) The sum of the amount or value of a qualifying distribution and such proportion thereof as corresponds to the rate of advance corporation tax in force for the financial year in which the distribution is made is in this Part of this Act referred to as "a franked payment," and references to any accounting or other period in which a franked payment is made are references to the period in which the distribution in question is made.

84(4) In this Part of this Act **"qualifying distribution"** means any distribution other than—

(a) a distribution which, in relation to the company making it, is a distribution by virtue only of

paragraph (c) of section 233(2) of the Taxes Act (bonus redeemable share capital and bonus securities); or

(b) a distribution consisting of any share capital or security which the company making the distribution has directly or indirectly received from the company by which the share capital or security was issued and which, in relation to the latter company, is a distribution by virtue only of that paragraph.

84(5) Schedule 14 to this Act shall have effect for the purpose of regulating the time and manner in which advance corporation tax is to be accounted for and paid.

SEC. 85 Payments of advance corporation tax to be set against company's liability to corporation tax on its income

85(1) Subject to subsection (2) below, advance corporation tax paid by a company (and not repaid) in respect of any distribution made by it in an accounting period shall be set against its liability to corporation tax on any income charged to corporation tax for that accounting period and shall accordingly discharge a corresponding amount of that liability.

85(2) The amount of advance corporation tax to be set against a company's liability for any accounting period under subsection (1) above shall not exceed the amount of advance corporation tax that would have been payable (apart from section 89 below) in respect of a distribution made at the end of that period of an amount which, together with the advance corporation tax so payable in respect of it, is equal to the company's income charged to corporation tax for that period.

85(3) Where in the case of any accounting period of a company there is an amount of surplus advance corporation tax (that is to say, advance corporation tax which cannot be set against the company's liability to corpora-

tion tax for that period because the company has no income charged to corporation tax for that period or because the company has no income charged to corporation tax for that period or because of subsection (2) above or subsection 100(6) below) the company may, within two years after the end of that period, claim to have the whole or any part of that amount treated for the purposes of this section (but not of any further application of this subsection) as if it were advance corporation tax paid in respect of distributions made by the company in any of its accounting periods beginning in the six years preceding that period (but so that the amount which is the subject of the claim is set, so far as possible, against the company's liability for a more recent accounting period before a more remote one) and corporation tax shall, so far as may be required, be repaid according.

85(4) Where in the case of any accounting period of a company there is an amount of surplus advance corporation tax which has not been dealt with under subsection (3) above, that amount shall be treated for the purposes of this section (including any further application of this subsection) as if it were advance corporation tax paid in respect of distributions made by the company in the next accounting period.

85(5) Effect shall be given to subsections (1) and (4) above as if on a claim in that behalf by the company and, for that purpose, a return made by the company under section 11 of the Management Act containing particulars of advance corporation tax or surplus advance corporation tax which falls to be dealt with under those subsections shall be treated as a claim.

85(6) For the purposes of this section the income of a company charged to corporation tax for any period shall be taken to be the amount of its profits for that period on which corporation tax falls finally to be borne exclusive of the part of the profits attributable to chargeable gains

or development gains; and that part shall be taken to be the amount brought into the company's profits for that period for the purposes of corporation tax in respect of chargeable gains or development gains before any deduction for charges on income, expenses of management or other amounts which can be deducted from or set against or treated as reducing profits of more than one description.

85(7) No advance corporation tax shall by virtue of this section be set against a company's liability to corporation tax charged for any time before 1st April 1973, and this section has effect subject to the subsequent provisions of this Act.

SEC. 86 Tax credit for certain recipients of qualifying distributions

86(1) Where a company resident in the United Kingdom makes a qualifying distribution after 5th April 1973 and the person receiving the distribution is another such company or a person resident in the United Kingdom, not being a company, the recipient of the distribution shall be entitled to a tax credit under this section (in this Part of this Act referred to as a "tax credit.".

86(2) The tax credit in respect of a distribution shall be available for the purposes specified in this section and the subsequent provisions of this Act, and shall be equal to such proportion of the amount or value of the distribution as corresponds to the rate of advance corporation tax in force for the financial year in which the distribution is made.

86(3) Subject to section 89(5) below, a company resident in the United Kingdom which is entitled to a tax credit in respect of a distribution may claim to have the amount of the credit paid to it if—

(a) the company is wholly exempt from corporation tax or is only not exempt in respect of trading income; or

(b) the distribution is one in relation to which express exemption (otherwise than by section 239 of the Taxes Act) is given, whether specifically or by virtue of a more general exemption from tax, under any provisions of the Tax Acts.

86(4) A person, not being a company resident in the United Kingdom, who is entitled to a tax credit in respect of a distribution may claim to have the credit set against the income tax chargeable on his income under section 3 of the Taxes Act or on his total income for the year of assessment in which the distribution is made and, where the credit exceeds that income tax, to have the excess paid to him.

86(5) Where a distribution mentioned in subsection (1) above is, or falls to be treated as, or under any provision of the Tax Acts is deemed to be, income of a person other than the recipient, that person shall be treated for the purposes of this section as receiving the distribution (and accordingly the question whether he is entitled to a tax credit in respect of it shall be determined by reference to where he, and not the actual recipient, is resident); and where any such distribution is income of a United Kingdom trust the trustees shall be entitled to a tax credit in respect of it if no other person falls to be treated for the purposes of this section as receiving the distribution.

GROUPS OF COMPANIES

SEC. 92 Setting of company's surplus advance corporation tax against subsidiary's liability.

92(1) Where a company (in this section referred to as "the surrendering company") has paid an amount of advance corporation tax in respect of a dividend or dividends paid by it in an accounting period and the advance corporation tax in respect of a dividend or dividends paid by it in an accounting period and the advance corporation tax has not been repaid, it may, on making a claim, surrender the benefit of the whole or part of that amount to any company which was a subsidiary of the surrendering company throughout that accounting period, or (in such proportions as the surrendering company may determine) to any two or more companies which were subsidiaries of the surrendering company throughout that period.

92(2) Subject to subsections (3A) and (4) below, where the benefit of any amount of advance corporation tax ("the surrendered amount") is surrendered under this section to a subsidiary, then—

(a) if the advance corporation tax mentioned in subsection (1) above was paid in respect of one dividend only or of dividends all of which were paid on the same date, the subsidiary shall be treated for the purposes of section 85 above as having paid an amount of advance corporation tax equal to the surrendered amount in respect of a distribution made by it on the date on which the dividend or dividends were paid;

(b) if the advance corporation tax mentioned in subsection (1) above was paid in respect of dividends paid on different dates, the subsidiary shall

be treated for the purposes of that section as having paid an amount of advance corporation tax equal to the appropriate part of the surrendered amount in respect of a distribution made by it on each of those dates.

92(3) For the purposes of paragraph (b) of section (2) above **"the appropriate part of the surrendered amount"** in relation to any distribution treated as made on the same date as that on which a dividend was paid, means such part of that amount as bears to the whole of it the same proportion as the amount of that dividend bears to the total amount of the dividends mentioned in that paragraph.

92(3A) No advance corporation tax which a subsidiary is treated as having paid by virtue of subsection (2) above shall be set against the subsidiary's liability to corporation tax under subsection (3) of section 85 above; but in determining for the purposes of subsections (3) and (4) of that section what (if any) amount of surplus advance corporation tax there is in any accounting period of a subsidiary, an amount so treated as having been paid shall be set against its liability to corporation tax before any advance corporation tax paid in respect of any distribution made by the subsidiary.

92(4) No advance corporation tax which a subsidiary is treated as having paid by virtue of subsection (2) above shall be set against the subsidiary's liability to corporation tax for any accounting period in which, or in any part of which, it was not a subsidiary of the surrendering company.

92(5) Any claim under this section shall be made within six years after the end of the accounting period to which it relates and shall require the consent, notified to the inspector in such form as the Board may require, of the subsidiary or subsidiaries concerned.

92(6) No amount of advance corporation tax which has been dealt with under subsection (3) of section 85 above shall be available for the purposes of a claim under this section; and no amount of advance corporation tax the benefit of which has been surrendered under this section shall be treated for the purposes of that section as advance corporation tax paid by the surrendering company.

APPENDIX C

[Joint Stipulation of the Parties, Paragraphs 19-23]

IN THE UNITED STATES CLAIMS COURT

No. 80-85T

XEROX CORPORATION,

v. *Plaintiff*

THE UNITED STATES,

Defendant

PARTIAL STIPULATION OF FACTS

It is hereby stipulated that, for the purposes of this case only, the following statements may be accepted as facts and all exhibits referred to herein and attached hereto are incorporated in this stipulation and made a part hereof, subject to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated.

* * * *

19. Except as provided in paragraph 21 below, ACT paid by a distributing corporation is not refundable by the U.K. to the corporation making the qualifying distribution or to the shareholders of such corporation.

20. Qualifying distributions made by a resident U.K. corporation must be reported on Form CT-61 to the Inland Revenue within: (i) 14 days after the close of a calendar quarter (i.e., March, June, September, December) for distributions made during such quarters; and (ii) if the accounting period of such U.K. resident corporation is other than the calendar year, within 14 days of the close of such accounting period for distributions made from the close of the prior calendar quarter to the close of the accounting period. With respect to any

qualifying distribution which requires the distributing company to make an associated payment of ACT, such ACT must be paid by the distributing company at the time the Form CT-61 is filed.

21. If a resident U.K. corporation makes a qualifying distribution in one calendar quarter and pays ACT with respect to such distribution, it may obtain a refund of such ACT from Inland Revenue if and to the extent it receives franked investment income during the remainder of the same accounting period.

22. The refund referred to in paragraph 21 above is the only circumstance by which a distributing company can obtain a refund of ACT paid, and such circumstance is the sole reason for the parenthetical "(and not repaid)" in section 85(1), FA 1972.

23. A resident U.K. corporation making a qualifying distribution which is not out of franked investment income must pay ACT regardless of its income and whether or not it has any U.K. corporation tax liability, which could be satisfied by use of the associated section 85 offset; thus, because of these reasons and because ACT is not refundable, ACT is not an "estimated tax" payment and is not similar to U.S. corporate estimated tax payments.

* * * *

[Signature]
MICHAEL C. DURNEY
Acting Assistant Attorney General

[Signature]
KENNETH C. GOBETZ
Attorney for Defendant

[Signature]
H. STEWART DUNN, JR.
Ivins, Phillips & Barker
Suite 600
1700 Pennsylvania Avenue, N.W.
Washington, D.C. 20006

Attorney for Plaintiff

APPENDIX D

[Post Trial Reply Brief of the United States (Cl. Ct.) at 3]

IN THE UNITED STATES CLAIMS COURT

No. 80-85T

XEROX CORPORATION,

Plaintiff

v.

THE UNITED STATES,

Defendant

REPLY OF THE UNITED STATES TO PLAINTIFF'S POST-TRIAL BRIEF

[January 14, 1988]

* * * *

Thus, without even addressing the technical legal arguments of the parties, a common sense approach to this case dictates the proper result. The disputed issue involves the interpretation of an agreement between the United States and the United Kingdom. The position of the United States in this litigation is grounded in the text of the Convention and the interpretation of the Convention explicitly accepted by the United Kingdom, the Senate, the Treasury, and the Internal Revenue Service.

APPENDIX E

[Excerpt from the Testimony of Norman C. England, Partner and Chartered Accountant, Peat Warwick Co., Transcript of Proceeding, the United States Claims Court, No. 80-85T, October 13, 1987 (trial transcript)]

MR. DUNN: And, Your Honor, if it's agreeable we will be referring to Rank Zerox Limited as RXL.

THE COURT: That's fine.

BY MR. DUNN:

Q: Is that correct, that you have represented them for a period of time?

A. That is correct.

Q. Have you had occasion to look at this exhibit [Resp. App. A, *supra,* 1a]?

A. I have.

Q. Does it, to the best of your knowledge, correctly represent the organization of the company in 1974?

A. Yes, that's a fair representation of its structure at that time.

Q. And from your experience which you testified to in representing American companies that were operating abroad, is this an unusual corporate structure for an American Company to have through its United Kingdom?

A. It is unusual as a corporate structure.

Q. Can you explain why, if you have a reason, why you think it is unusual?

A. It is unusual, Your Honor, for a United States parent company with subsidiary companies overseas to use that form of structure.

Because that structure predominantly involves Xerox Corporation owning various subsidiary companies outside the United Kingdom indirectly through RXL.

That is an unusual because orthodox of a group structure would avoid ownership of that sort. And the reason why one would wish to avoid ownership of that sort is because the ownership of foreign companies by Xerox

Corporation and via a United Kingdom company tends to create the possibility of the overall burden of taxation increasing by reason of profits needing to flow from territories outside the United Kingdom through the United Kingdom onto the United States.

And at the time that such profits pass through the United Kingdom, some measure of United Kingdom taxation tends to be created.

For that reason, more orthodox planning of the group structure would have led to the Untied States parent company, in this instance Xerox Corporation, owning its overseas subsidiaries other than RXL directly rather than via RXL.

Q. Mr. England, do I understand or could your testimony be illustrated by the following? Let's say the tax rate on corporate profits in Sweden is 20 percent?

A. Yes.

Q. And the tax rate on corporate profits at the time in the United Kingdom is 50 percent?

A. Yes.

Q. Now if the earnings in the Swedish company flow by dividends by Xerox through RXL then to Xerox, are you saying that produces a tax disadvantage?

A. I'm saying it potentially produces a disadvantage because it will increase the burden of taxes outside the United States.

On that illustration from 20 percent to 50 percent in broad terms.

Q. And your further testimony, that normally American corporations would own the subsidiaries of these major countries directly?

A. It is my testimony that, that would have been the more orthodox form of group structure.

Q. Do you know why Xerox did not follow the more orthodox procedure?

A. Yes, I do, Mr. Dunn. It may help the Court, Your Honor, if I explain something of the historical background to RXL briefly.

A few years after the war, Xerox Corporation, which was then a much smaller company than it is now had an ability to exploit a copying process and was minded to exploit it in the European market.

At that time, Xerox Corporation didn't have the capacity to do that relying exclusively upon its own management in Europe.

And it emerged that what happened was that Xerox Corporation and Rank Organization Limited combined together to form and own RXL.

The reason why the Rank Organization Limited was brought into this joint ownership was that the Rank Organization Limited at that time and indeed today, did have a substantial presence with management in Europe.

So that when RXL started, and I think it was within a year or two around 1950 as an effective commercial entity, the dominant management contribution to its affairs was provided by the Rank Organization Group rather than by Xerox Corporation.

And although at that time the equity interests in RXL of Xerox and of Rank Organization were equal, the wishes of the Rank Organization tended to be adhered to rather than Xerox Corporation wishes in the evolution of the corporate structure.

APPENDIX F

[Brief of the United States (Claims Court), p. 31 (July 8, 1987)]

* * * *

The double crediting problem described in the previous section could, in theory, be resolved in one of two ways. Either the Article 23(1)(a) credit could be limited to the amount of cash paid to satisfy corporation tax liability, or the 23(1)(c) credit could be reversed once the 23(1)(a) credit is granted.

[Brief of the United States (Federal Circuit), pp. 42-3 (June 23, 1993)]

In summary, Article 23(1) can be interpreted as providing two foreign tax credits for a single payment of tax to the U.K. Taxpayer has offered an explanation as to how the double crediting problem can be avoided, that is, by allowing a credit under Article 23(1)(a) only for the balance of corporation tax that is paid after the application of ACT payments for which a credit has been given under Article 23(1)(c). The U.S. Government agency responsible for enforcing the Treaty, the Department of the Treasury, has offered an alternative explanation, to wit, that once ACT is applied towards the satisfaction of U.K. corporation tax liability the Article 23(1)(c) credit is to be reversed and all payments used to satisfy the U.K. corporation tax, including ACT payments, become creditable under Article 23(1)(a).

APPENDIX G

[Treas. Reg. § 1.901-2(e)(4)]

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(4) Multiple levies. (i) In general. If under foreign law, a taxpayer's tentative liability for one levy (the "first levy") is or can be reduced by the amount of the taxpayer's liability for a different levy (the "second levy"), then the amount considered paid by the taxpayer to the foreign country pursuant to the second levy is an amount equal to its entire liability for that levy, and the remainder of the amount paid is considered paid pursuant to the first levy. This rule applies regardless of whether it is or is not likely that liability for one such levy will always exceed liability for the other such levy. For an example of the application of this rule, see example (5) of § 1.903-1(b)(3). If, under foreign law, the amount of a taxpayer's liability is the greater or lesser of amounts computed pursuant to two levies, then the entire amount paid to the foreign country by the taxpayer is considered paid pursuant to the levy that imposes such greater or lesser amount, respectively, and no amount is considered paid pursuant to such other levy.

APPENDIX H

[Senate Executive Report No. 95-18, 95th Cong., 2d Sess. 37]

REPORT

OF THE

COMMITTEE ON FOREIGN RELATIONS

UNITED STATES SENATE

ON

TAX CONVENTION WITH THE UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND; EXECUTIVE Q, 94TH CONG., 2D SESS., FIRST PROTOCOL TO THE TAX CONVENTION WITH THE UNITED KINGDOM; EXECUTIVE J, 95TH CONG., 1ST SESS., SECOND PROTOCOL TO THE TAX CONVENTION WITH THE UNITED KINGDOM

April 25, 1978.—Ordered to be printed

* * * *

The ACT refunds, the withholding tax, and the unrefunded portion of the ACT are treated for U.S. foreign tax credit purposes in a manner which is generally favorable to U.S. shareholders. These rules raise difficult and complex issues. In recommending the ratification of the proposed treaty, the Committee does not intend that these rules necessarily serve as a model for future treaties. Further, in recommending the ratification of the treaty, the Committee does not intend to adopt or reject the amplifications of the foreign tax credit rules contained in the Treasury technical explanation. Consequently, Treasury would not be foreclosed by the ratification of the treaty from modifying those administrative interpretations in the future should it deem it advisable to do so. Of course, the rules contained in the treaty also do not limit any legislative action in this area; the computation of the foreign tax credit for unrefunded ACT may be subject to any generally applicable changes in the U.S. foreign tax credit rules which may subsequently be enacted.

* * * *

APPENDIX I

[Letter of United Kingdom, Inland Revenue to Xerox' Counsel, dated May 9, 1989]

[Inland Revenue letterhead]

Mr. H Stewart Dunn Jr.
Ivins, Phillips & Barker
1700 Pennsylvania Avenue NW
Washington DC 20006
USA

9 May 1989

Dear Mr. Dunn

RE: XEROX CORP. v. UNITED STATES
Cl. Ct. No. 80-985T (1974)

In your letter of April 27 1989 you asked Inland Revenue to let you know the official position of the United Kingdom on cetrain specific matters. By way of background to our response, we have reviewed the Opinion of Judge Futey of March 17 1988, the briefs submitted to the Court by the United States Department of Justice and relevant portions of the transcript in the case. We have had several meetings with you, other representatives of Xerox, and their United Kingdom advisers. I have noted your reference to the exchanges referred to in the first paragraph of your letter.

Before responding to your inquires, I wish to make two points clear. First, we cannot take sides in the Xerox litigation in the United States. Second, we cannot and do not express opinions on any matters of United States law.

Turning to the specific inquires in your letter of April 27 1989, you have asked us to inform you whether we received from the United States copies of either the

original (March 9 1977) or the revised (July 25 1977) United States Treasury Technical Explanation of the United Kingdom/United States Double Tax Treaty of December 31 1975. You further asked whether we have explicitly or implicitly approved either or both of those Technical Explanations.

We are not prepared to answer your first inquiry because to inform you whether we received such documents would be a departure from our normal confidentiality practice and convention. Assuming, however, that we had received such documents (without suggesting that we did or did not receive them), your second inquiry is whether the receipt of either or both of such documents constituted explicit or implicit acceptance of them by the United Kingdom. We do not understand how the receipt of documents can constitute explicit acceptance of them or of their contents. Whether the receipt of documents would constitute implicit acceptance seems to us to depend on the circumstances. In so far as the answer to this question depends on the interpretation of United States law, we have no comment. As a matter of United Kingdom law our view would be that receipt alone would not constitute acceptance. Certainly, ratification of the Treaty by the United Kingdom did not constitute acceptance by the United Kingdom of anything other than the terms of the Treaty itself.

You have also inquired as to whether these Technical Explanations would have been before the House of Commons on any of the occasions when it considered the United Kingdom/United States Double Tax Treaty. This matter is addressed in the affidavits of Lord Rees and the Right Hon Denzil Davies M.P.

You also asked whether we have explicitly or implicitly accepted certain positions of the United States Internal Revenue Service stated in Rev. Proc. 80-18, 1980-1 CB 623 (April 25, 1988). We consider such statements of the Internal Revenue Service to be matters which are not

the responsibility of the United Kingdom Government. There would, therefore, be no question of our having explicitly accepted or approved Rev. Proc. 80-18 and the positions taken therein. The position as to implicit acceptance depends, of course, on the application of the relevant legal principals. We can state, however, that we are not conscious of having said or done anything which would amount to implicit acceptance in United Kingdom law.

You have asked us to review certain earlier correspondence relating to this same general subject and to advise you whether the positions stated in that correspondence remain the position of the Inland Revenue. Also, you have asked whether the statements made in these earlier documents with respect to Article 10(2) are also applicable to Article 23(1). The correspondence to which you refer are the following letters:

1. N C England to R W Parker of 20 October 1981;
2. R W Parker to N C England of 26 October 1981;
3. Peat, Marwick, Mitchell & Co to J F Hall of 17 April 1986; and
4. J F Hall to Peat, Marwick, Mitchell & Co of 21 April 1986.

Copies of this correspondence were attached to your letter and are appended hereto for further reference.

Since the above correspondence took place, the interpretation of Article 10 has been considered in the Judgment of Mr. Justice Harmon in the High Court of Justice in *Union Texas Petroleum Corp. v. Derek John Critchley (HM Inspector of Texas)* 1988 STC 691. There does not appear to be anything in that Judgment which conflicts with the views confirmed in this correspondence which, therefore, remains the position of the Inland Reve-

nue. As regards the application to Article 23(1) I would refer you to the relevant provisions of the Competent Authority Agreement of 18/23 December 1986.

As a senior official of the Inland Revenue, being the Director of the International Division of the Inland Revenue, I am authorised to write this letter on behalf of the Commissioners of Inland Revenue of the United Kingdom.

It is understood between us that no action will be taken by you on this letter for ten working days from the date of this letter.

Yours sincerely

[Signature]
BRIAN HOUGHTON
DIRECTOR OF INTERNATIONAL DIVISION
INLAND REVENUE
[U.K. Competent Authority]

[Letter of United Kingdom, Inland Revenue to Xerox' Counsel, dated July 31, 1992]

[Inland Revenue letterhead]

Mr. H Stewart Dunn Jr.
Ivins, Phillips & Barker
1700 Pennsylvania Avenue NW
Washington DC 20006
USA

31 July 1992

Dear Mr. Dunn

RE: XEROX CORP. *v.* UNITED STATES
Cl. Ct. No. 80-85T (1974)

Brian Houghton, the former Director of this Division, wrote to you on 9 May 1989 in reply to a letter from you of 27 April 1989. You wrote to me on 30 July 1992 asking some further questions.

Before responding to your enquiries, I wish to make two points clear (as Brian Houghton did on 9 May 1989). First, we cannot and do not express opinions on any matters of United States law. Second, we cannot take sides in the Xerox litigation in the United States.

Turning now to the specific enquiries you make, you ask first whether either the original or the revised United States Treasury Technical Explanations were, or are, part of the negotiated double taxation agreement with the United Kingdom. So far as the United Kingdom is concerned, the negotiated agreement between the United Kingdom and the United States consists only of the double taxation convention and its amending protocols. In so far as the answer to this question depends upon the interpretation of US law, we have no comment.

You asked second about the relationship between Article 23(1)(c) and Article 10(2)(a)(i) of the double taxation agreement referred to in the competent authority

agreement of 18-23 December 1986. This is set forth in paragraph 1 of that agreement which reads as follows:

"1. It is agreed that Article 23(1)(c) provides a mechanism by which a US foreign tax credit may be obtained for that part of the UK tax credit referred to in Article 10(2)(a)(i) which is not paid to a US corporation but to which an individual resident in the United Kingdom would have been entitled had he received the dividend."

With respect to your third question the Inland Revenue has nothing to add—and has added nothing—to the terms of the competent authority agreement. Those terms speak for themselves and any interpretation put, or sought to be put, on them is the sole responsibility, and will reflect only the views, of those who put, or advance, that interpretation.

You asked fourth whether either of the United States Treasury Technical Explanations were presented to the House of Commons. This is a matter of public record and we have no reason to dissent from the statements as to this made by Lord Rees and Mr. Denzil Davies in their affidavits.

I confirm that Brian Houghton's letter of 9 May 1989 remains the position of the Inland Revenue on the subject matter covered by that letter and that I am authorised to write this letter on behalf of the Commissioners of Inland Revenue of the United Kingdom.

It is understood between us that no action will be taken by you on this letter for 10 working days from the date of this letter.

Yours sincerely,

[Signature]
P W FAWCETT
Assistant Secretary
International Division
Inland Revenue
[U.K. Competent Authority]

APPENDIX J

[Treasury Department Conference of April 24, 1980 on the Issuance of Revenue Procedure 80-18]

CONFERENCE REPORT

1. Name of Taxpayer
   Rev. Proc. 80-18 re U.S.-U.K. Income Tax Convention

2. Time Consumed
   45 min

3. Subject of Conference
   Transfer of Advance Corporation Tax (ACT)

4. Date, Time and Place
   4-24-80
   4:30 p.m.
   Room 3302

5. Name(s) of Taxpayer or Representative(s) attending Conference
   Treasury conferees: Mr. Lubick (X)
   Mr. Rosenbloom (XLI)
   Mr. Hannes (XLI)

6. IRS Conferees:
   The Commissioner
   Mr. O'Connor (CStaff)
   Mr. Portney (A/C(T))
   Mr. Cohen (CC)
   Mr. Stein (CC)
   Mr. Sebastian (CC:INT)
   Mr. Goldwag (T:C)
   Mr. Rassmussen (CC:INT)
   Mr. Watson (CC:INT)
   Mr. Hotine (CC:INT)
   Mr. Lieberman (T:C:C:3:1)
   Mr. Levy (T:C:C:P:1)

7. Brief Resume of Conference, Including Conclusions Reached (List Code sections involved)

The conference was convened for the purpose of expressing to the Commissioner the concerns that T:C had with respect to the treatment in the revenue procedure for purposes of the indirect credit under section 902 of the Code of the "surrender" of the ACT payment by a U.K. parent to one or more of its subsidiaries under section 92 of the U.K. Finance Act of 1972 so that the Commissioner could decide whether this should be the Service's published position on this issue. Time was of the essence since the new Convention enters into force on 4-25-80 and it was hoped that the revenue procedure would be released on the same day.

The surrender system referred to above is the U.K.'s way of achieving a partial consolidation of related corporations for purposes of taxation, somewhat analogous to the U.S. consolidation system. Under this system, the U.K. parent (usually a holding company with no mainstream tax liabiilty) may transfer to a related U.K. corporation (usually an operating sub) the right to apply ACT paid by the parent to its mainstream tax liability. Section 3.05 of the revenue procedure treats the sub as having paid the unrefunded ACT offset against the sub's mainstream tax and treats the parent as having contributed to the capital of the sub an amount equal to the unrefunded ACT offset.

T:C's concern with respect to the treatment of the ACT surrender is that, although the policy considerations for such treatment may be great, there is a question as to whether there is sufficient legal authority for such treatment. The new Convention does not address this issue, notwithstanding the fact that the underlying theme of the Technical Explanation of the Convention is that ACT follows mainstream tax with respect to years of offset and the corresponding earnings and profits (presumably and impliedly of the U.K. corporation paying the ACT). Such treatment arguably is inconsistent with the holding in *Biddle v. Commissioner*, 302 U.S. 573, 1938-1 C.B.

309, with respect to who the taxpayer is for foreign tax credit purposes.

Treasury agreed that there may be a question of consistency with *Biddle* regarding the treatment of the surrender in revenue procedure. However, in *Biddle* the question of who the taxpayer was for credit purposes was whether it was the U.K. corporation for section 902 purposes or the U.S. shareholder for section 901 purposes. Here the question is whether the taxpayer is the U.K. parent or the U.K. sub for section 902 purposes. The revenue procedure, in effect, focuses on who pays the mainstream tax rather than who pays the ACT, since the ACT is really an advance payment corporate tax, analogous in many ways to the U.S. estimated tax payment. The revenue procedure recognizes that under the U.K. surrender system, the U.K. parent is, in effect, paying its subsidiary's tax liability on behalf of the subsidiary, which treatment is apparently consistent with the proposed section 901 regulations. Treasury further explained by way of an example that the treatment in the revenue procedure prevents a U.K. parent from amassing fictitious excess credits resulting from non-U.K. income that would shelter other tax haven income. Treasury did, however, concede that the revenue procedure treatment is an open issue and that some taxpayers could object and possibly win in court, but that it is a situation that both the Service and Treasury are aware of and that we should take a shot at remedying by taking this position, which is as reasonable as the contrary position.

The Commissioner agreed and approved the publication of the revenue procedure and thanked T:C for having informed him of the problems involved.

(Reverse Side of Printed Form Omitted)

APPENDIX K

[Affidavit of Robert J. Patrick, Jr.; Joint Stipulation in Lieu of Testimony]

IN THE UNITED STATES CLAIMS COURT

No. 80-85T

XEROX CORPORATION,

Plaintiff

v.

THE UNITED STATES,

Defendant

STIPULATION IN LIEU OF TESTIMONY

The parties hereby stipulate and agree, in lieu of the live testimony or other submission by Robert J. Patrick, that the following affidavits, dated June 8, 1987, and August 21, 1987 would constitute the entire substance of the testimony of Robert J. Patrick if he were called at trial to testify in the above-referenced matter, and that the same may be introduced and received in evidence (without objection, except as to relevance). By entering into this stipulation the United States does not thereby stipulate to the truth of the statements herein.

Respectfully submitted,

Date: ———

[Signature]
H. STEWART DUNN, JR.
IVINS, PHILLIPS & BARKER
Suite 600
1700 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
Attorney for Plaintiff

Date: [10/8/87]

[Signature]
MICHAEL C. DURNEY
Acting Assistant Attorney
Attorney General

Date: [10/8/87]

[Signature]
KENNETH C. GOBETZ
Trial Attorney
Department of Justice (Tax)
Claims Court Section
Post Office Box 26
Ben Franklin Post Office
Washington, D.C. 20044
(202) 724-6500
Attorney for Defendant

AFFIDAVIT

I, ROBERT J. PATRICK, JR., swear and affirm that the following is true and accurate to the best of my knowledge.

Since submitting my affidavit of June 8, 1987 in the pending litigation of Xerox Corp. v. United States, Cl. Ct. No. 80-85T, I have reviewed the pretrial brief of the United States in this litigation which was filed on July 8, 1987. Since that brief presents an analysis of Article 23 of the United States-United Kingdom Income Tax Treaty which was not considered by me in my affidavit of June 8, 1987, I believe it is necessary to supplement that affidavit in order fully and correctly to present my views on the terms of the treaty.

The government's brief adopts the position that Article 23(1)(c) provides a credit for ACT on only an interim basis and that the permanent credit for ACT is provided only by Article 23(1)(a). To the best of my knowledge, this interpretation of the Treaty has never previously been set forth by the United States, the United Kingdom or anyone else. The United States foreign credit for amounts not refunded under Article 10(2)(a)(i) is provided by Article 23(1)(c) and the credit for United Kingdom corporation tax under Article 23(1)(a) is for a net credit after reduction by ACT.

[Signtaure]
ROBERT J. PATRICK, JR.

[Notary Omitted in Printing]

APPENDIX L

[Affidavit of Rt. Hon. Denzil Davies PC., M.P.]

UNITED STATES CLAIMS COURT

Cl. Ct. No. 80-85T

XEROX CORPORATION,

Plaintiff

v.

THE UNITED STATES,

Defendant

AFFIDAVIT OF THE RIGHT HONOURABLE DENZIL DAVIES PC., M.P.

United Kingdom) ss 4, Raymond Buildings
) Gray's Inn
) City of London
) London W.C.1

I, THE RIGHT HONOURABLE DAVID JOHN DENZIL DAVIES of 4, Raymond Buildings, Gray's Inn, London W.C.1. MAKE OATH and SAY as follows:

1. I have a Bachelor of Arts Degree from Oxford University where, in 1962, I obtained First Class Honours in Law. In 1963 I was a Teaching Fellow at the University of Chicago. In 1964 I was called to the Bar of England and Wales where I practised in the field of Revenue Law, until June 1975. I have now recently returned to practice at the Bar.

2. In 1970 I was elected Member of Parliament for the Parliamentary Constituency of Llanelli, a seat which I have held ever since and still hold.

3. Throughout my Parliamentary career I have been interested in financial and revenue matters, and I have been closely concerned with them on many occasions. One of those occasions was my membership of the Select Committee of the House of Commons which was appointed in May 1971 to consider the Green Paper on Reform of Corporation Tax which had been presented to Parliament by the then Chancellor of the Exchequer in March 1971. This report led to the imputation system which was enacted in the Finance Act 1972. I was appointed Minister of State at the Treasury in 1975 and held office until 1979 when the Labour Government of Mr. James Callaghan was defeated in the General Election held in May of that year.

4. Following the adoption of the imputation system in the Finance Act 1972, the Double Tax Treaty between the United Kingdom and the United States of American was renegotiated, and the bulk of this renegotiation took place while I was Minister of State at the Treasury in the Labour Governments which held office from February 1974 to May 1979.

5. The Treaty in its original form was entered into on 31st December 1975 and was amended by the Exchange of Notes of 13th April 1976 and the three Protocols of 26th August 1976, 31st March 1977 and 15th March 1979. All these events took place while I was Minister of State at the Treasury, but the Treaty, as so amended, was not finally approved and given effect as a matter of the domestic law of the United Kingdom until 1980 when The Double Taxation Relief (Taxes on Income) (The United States of America) Order 1980 was made on 25th April 1980 following its approval by the House of Commons on 18th February 1980. This long delay between the original agreement at the end of 1975 and final approval of the Treaty in 1980 was largely caused by the unitary tax issue. As originally agreed, Article 9(4) of the Treaty would have prohibited the

application of the unitary basis of taxation by both the Government of the United States and the individual States. However, this provision was unacceptable to the United States Senate which entered a reservation, upon Article 9(4), and which refused to approve the Treaty until Article 9(4) had been amended by the Third Protocol to limit its scope to the United States Federal Government.

6. Nevertheless, so far as the United Kingdom was concerned, the Treaty as amended by the Exchange of Notes and the First Protocol was approved by the House of Commons in a debate which took place on 12th January 1977. As I have stated above, at that time I was Minister of State at the Treasury, and as such I was the Government Minister responsible for the Treaty, and it was in that capacity that I opened and concluded the debate on the approval motion in the House of Commons. My speeches are reported in the extract from Hansard (see columns 1573 and following and 1597 and following) which is attached hereto as Exhibit 1. In the event, because of the unitary tax issue, the Senate of the United States of America declined to ratify the Treaty in the form in which it had been approved by the House of Commons in January 1977. Further amendments had to be negotiated, in particular in the Third Protocol which was entered into on 15th March 1979, before the Treaty was in a form acceptable to the United States Senate. Before the Treaty as so amended could be placed before the House of Commons, the Labour Government of Mr. James Callaghan (as he then was) of which I, as the Minister of State at the Treasury, was a member was defeated in the General Election of May 1979. Accordingly, it fell to my successor, Mr. Peter Rees (as he then was) as the Minister of State at the Treasury in the Conservative administration of Mrs. Margaret Thatcher to introduce the debate in the House of Commons which took place in February 1980 at which the Treaty as so amended, and the Order to incorporate it into the domestic law of the United Kingdom, The Double Taxation

Relief (Taxes on Income) (The United States of America) Order 1980, were approved by the House of Commons.

7. I am informed that issues have arisen between Xerox Corporation and the United States as to the effect of Article 23(1) of the Treaty. In this respect I have read the Opinion of Judge Futey filed on March 17, 1988 ("the Opinion") in the United States Claims Court in the case of *Xerox Corp. v. United States,* No. 80-85T ("the Case") with respect to the claim of Xerox Corporation to be entitled to an indirect United States foreign tax credit under Article 23(1) of the Treaty, and in particular the following statement which appears on page 16 of the Opinion:

> "Similarly, the record indicates at least tacit acceptance by the U.K. of the U.S. interpretation of Article 23(1)(c) as set forth in the Technical Explanation. As stated in the affidavit of Steven P. Hannes, who was a member of the U.S. negotiation team in 1975 and an Attorney for Treasury during the U.S. Senate's consideration of the treaty, "copies of the Technical Explanation would have been sent to the U.K. negotiators." Knowledge of the U.S. interpretation, therefore, was clearly before the House of Commons during its own ratification debate."

I have also been provided with copies of the original and the revised United States Treasury Technical Explanation of the Treaty and have read this material. I am informed that the Technical Explanation was published in the United States by the United States Treasury in its original form in March 1977 and in its revised form in July 1977, that is after the debate in the House of Commons on 12th January 1977 to which I have referred above.

8. I have been asked by Xerox Corporation whether I was aware of the Technical Explanation in either its

original or its revised form at the time of the debate in the House of Commons on 12th January 1977. I can state from my own knowledge that during the whole of the period when I was a Minister of State responsible for the Treaty, I had no knowledge of and never saw the United States Treasury Technical Explanation of the Treaty in any form. I was not aware of its existence and had no knowledge of its contents until it was shown to me by Xerox Corporation when I was first consulted with respect to this matter in January 1989. Therefore, I can categorically say that the statements of Judge Futey quoted in paragraph 7 above are not correct.

9. My attention has been drawn to two places in the Opinion where Judge Futey states that the United Kingdom Government accepted, at least tacitly, the United States Government's interpretation of Article 23(1)(c) as set forth in the Technical Explanation. These statements are at Opinion p. 16 ("Similarly, the record indicates at least a tacit acceptance by the U.K. of the U.S. interpretation of Article 23(1)(c) as set forth in the Technical Explanation.") and this point is repeated at Opinion p. 25. I have been asked to state whether the United Kingdom Government of which I was a member did, in fact, tacitly accept the United States interpretation of Article 23(1)(c) as set forth in the revised United States Technical Explanation. The answer is that the United Kingdom Government of which I was a member and on whose behalf I was the responsible Minister in this matter did not accept the United States Treasury's Technical Explanation either explicitly or implicitly.

10. Nor was I aware of the existence or the contents of Rev-Proc 80-18 in any form until it was shown to me by Xerox Corporation in January 1989.

11. In conclusion I would add that I always regarded the 1975 Treaty as a determined effort by both the United Kingdom and the United States to have a conven-

tion which was fair to both countries with terms that were properly balanced, and I so stated in the speech with which I opened the debate in the House of Commons on 12th January 1977, the official transcript of which is attached hereto as Exhibit 1 (my above remarks are to be found at column 1576). I also referred to the parity of treatment between the United Kingdom and the United States in my closing speech in the following passage which is to be found at column 1603:

> "A United Kingdom portfolio investor in the United States will suffer a 15 per cent. withholding tax. A United Kingdom direct investor in the United States will suffer a 5 per cent. withholding tax. A United States portfolio investor in this country will get the full tax credit which a United Kingdom resident would get in relation to corporation tax, less a 15 per cent. withholding tax. A direct investor in this country—which is where the argument has arisen about the imputation system—will get half the tax credit, or 17.5 instead of 35, less a 5 percent. withholding tax on the total. So we have gone half way in relation to direct investment. We have not gone the whole way. We have gone the whole way with portfolio investment. But there is parity of treatment between us and the United States."

[Signature]
DAVID JOHN DENZIL DAVIES

[Notary Omitted in Printing]

APPENDIX M

[Affidavit of the Lord Rees, PC., Q.C.]

UNITED STATES CLAIMS COURT

Cl. Ct. No. 80-85T

XEROX CORPORATION,

Plaintiff

v.

THE UNITED STATES,

Defendant

AFFIDAVIT OF THE RIGHT HONOURABLE THE LORD REES PC., Q.C.

United Kingdom) ss 11 New Square
) Lincoln's Inn
City of London) London W.C.2.

I, THE RIGHT HONOURABLE PETER WYNFORD INNES, THE LORD REES, of 11 New Square Lincoln's Inn London WC2 MAKE OATH and SAY as follows:

1. I have a Master of Arts Degree from Oxford University. I was called to the English Bar in 1957. Since 1957 I have practised exclusively in the field of taxation law, and I became Queens' Counsel in 1969.

2. In 1970 I was elected Member of Parliament for the Parliamentary Constituency of Dover, a seat which I held continuously until my retirement as a sitting member of the House of Commons at the dissolution of Parliament in 1987. Following my election as a Member of Parliament, I was a member of the Select Committee

of the House of Commons which in 1971 was charged with the task of reviewing various alternative systems of corporate taxation and which submitted a report to the House of Commons on 20th October 1971 recommending the imputation system prior to the adoption by the United Kingdom of that system of taxation upon the enactment of the Finance Act 1972. A copy of this report is attached as Exhibit 1.

3. When the Conservative Party under the leadership of Mrs. Margaret Thatcher won the General Election 1979, I became a member of the Government and served as Minister of State at the Treasury until 1981. From 1981 to 1983 I served as Minister for Trade. From 1983 to 1985, I served as Chief Secretary to the Treasury and a member of the Cabinet. In 1983 I was appointed a member of the Privy Council. I retired from the House of Commons in 1987 and was made a Life Peer in the Dissolution Honours of that year and became a member of the House of Lords.

4. During 1979 to 1981 as Minister of State at the Treasury, I was the Government Minister primarily charged with the conduct under the Chancellor of the Exchequer of revenue matters. It was in this capacity that I was responsible (together with the Chief Secretary to the Treasury) for the passage through Parliament of the first Finance Bill of Mrs. Thatcher's administration, the Finance Bill (No. 2) 1979. One of the Clauses in this Bill was Clause 16 (United States Double Taxation Convention), for which I was responsible, and which was enacted as Section 16 of the Finance Act (No. 2) 1979 when that Bill became law upon receiving the Royal Assent on 26th July 1979.

5. It was also in my capacity as Minister of State at the Treasury that I was responsible in 1980 for the laying before the House of Commons of the Order in Council to give effect as a matter of United Kingdom domestic

law to the 1975 Double Tax Convention between the United Kingdom and the United States of America ("the Treaty"), which had been signed on 31st December 1975 and amended by an Exchange of Notes dated 13th April 1976 and by three Protocols dated 26th August 1976, 31st March 1977, and 15th March 1979, respectively. The Order in Council was approved by the House of Commons on 18th February 1980, and after laying before the House for the requisite period under what is known as "the affirmative resolution procedure" was finally made on 21st April 1980 as Statutory Instrument 1980/568 (The Double Taxation Relief (Taxes on Income) (The United States of America) Order 1980). The Treaty then entered into force in accordance with Article 28(2) on 25th April 1980, instruments of ratification of the Treaty having been exchanged in Washington, D.C. on 25th March 1980.

6. I have read the Opinion of Judge Futey filed on March 17, 1988 ("the Opinion") in the United States Claims Court in the case of *Xerox Corp. v. United States*, No. 80-85T ("the Case") with respect to the claim of Xerox Corporation to be entitled to an indirect United States foreign tax credit under Article 23(1) of the Treaty.

7. I have been asked by Xerox Corporation to comment on certain statements in the opinion of Judge Futey of March 17, 1988 which are directed to the position of the United Kingdom Government. The first such statement is: "Knowledge of the United States interpretation, therefore, was clearly before the House of Commons during its own ratification debate. Opinion p. 16. I can state from my own knowledge as the Minister personally responsible for the legislation referred to in paragraphs 4 and 5 above that this statement is wholly incorrect, and that at no time was the United States interpretation in any way before the House of Commons. I note that:

(a) Although I was the government minister who introduced Clause 16 of the Finance Bill (No. 2) 1979 in the House of Commons in 1979 and presented the Treaty to the House of Commons for final consideration and approval in 1980, I was not aware of the existence of the United States Treasury Technical Explanation of the Treaty or of Rev. Proc. 80-18, and had no knowledge of their contents, until these were shown to me by Xerox Corporation when I was first consulted with respect to this matter in July 1988.

(b) In October 1988, I went to the Treasury in London and there read all the files submitted to me in 1979 and 1980 when I was Minister of State at the Treasury in connection with the Treaty and its three Protocols. Those papers did not contain the Technical Explanation or any other papers emanating from the United States Treasury or Internal Revenue Service giving the view of the United States as to the construction of the Convention.

(c) I also went in October 1988 to the Library of the House of Commons to see whether the Library had any record of the Technical Explanation or any equivalent paper having been placed there prior to the relevant debates or at any other time. The Library contained no such record.

Having confirmed my memory by the research referred to above, I can say categorically that I was not at any time as Minister or as a Member of the House of Commons shown the Technical Explanation, or briefed on the Technical Explanation or the point at issue in the Case. Since I was the responsible Government Minister speaking for the Government in the debates before the House of Commons, I would be the only person to bring any such material before the House of Commons or authorise it to be deposited in the library of the House of Commons.

8. The second statement on which I have been asked to comment is the sentence immediately following the

statement quoted and discussed in paragraph 7 above, which is: "The U.K. ratified the Convention in the form approved by the U.S. Senate without further reservation or amendment, by enacting section 16 of the Finance Act (No. 2) 1979, dated July 26, 1979." Section 16 was an "enabling" and not a ratification provision. In any event, Section 16 of the Finance Act (No. 2) 1979 did not in any way affirm, adopt or ratify the United States Treasury interpretation of the Treaty, and as previously stated, the United States Treasury's interpretation of the Treaty was not before the House of Commons when it approved Section 16 or subsequently when it approved the Treaty.

9. In two places in his opinion Judge Futey states that the United Kingdom Government accepted, at least tacitly, the United States Government's interpretation of Article 23(1)(c) as set forth in the Technical Explanation. These statements are at Opinion p. 16 ("Similarly, the record indicates at least a tacit acceptance by the U.K. of the U.S. interpretation of Article 23(1)(c) as set forth in the Technical Explanation.") and this point of tacit acceptance is repeated at Opinion p. 25. I have been asked to state whether the United Kingdom Government did, in fact, tacitly accept the United States interpretation of Article 23(1)(c) as set forth in the revised United States Technical Explanation. The answer is that the United Kingdom Government did not accept this United States Treasury Technical Explanation of Article 23 either explicitly or implicitly. For the reasons stated in detail in paragraphs 7 and 8 above, the United States Treasury's Technical Explanation was not before, and its very existence was not known by the House of Commons nor by me as the responsible government minister.

10. Finally I have been asked to comment on the following statements in Judge Futey's Opinion:

> (1) "In view of the United Kingdom's subsequent ratification of the Convention without reservation, and with full knowledge of the Technical Explana-

tion underlying the U.S. ratification, it is difficult to sustain Plaintiff's assertion that the Technical Explanation did not conform with the terms of the treaty." Opinion p. 22

(2) "The Technical Explanation formed the basis of the Senate's intent in ratifying the Convention, and no objection thereto was voiced by the U.K. prior to its own ratification." Opinion p. 27.

As I have already explained above, when the United Kingdom House of Commons approved the Order in Council giving effect to the Treaty as a matter of U.K. domestic law in February 1980, neither it nor I as the Minister responsible had any knowledge, express or implied, of the Technical Explanation. In these circumstances, it is not surprising that the United Kingdom voiced no objection to the Technical Explanation.

11. In addition, I have been asked to comment on a statement of mine from a January 1977 debate in the House of Commons which is quoted in part in the Pretrial Brief of the United States dated July 8, 1987 at page 48, footnote 38. This quote and a further reference to this footnote in the Post-Trial brief of the United States at page 12, footnote 10, are used to support the argument that the United Kingdom had knowledge of, and apparently accepted, the United States Treasury's interpretation of Article 23(1) in the Technical Explanation. At the time of this January 1977 debate I was the principal front bench spokesman on revenue matters for the Conservative Party, which was then in opposition to the ruling Labour Party. As such, I participated in the debate in the House of Commons and my speech is reported in the extract from Hansard (the official transcript) which is attached as my Exhibit 2 (see column 1585 and following). It is an extract from this speech of mine which is quoted in the brief of the United States as follows:

> "We understand that there are regular meetings between the United States Internal Revenue Service and the Inland Revenue."

This quote is the first sentence of the fourth complete paragraph in column 1586 of the Hansard Report. It is clear from the context in which this statement appears that I made these remarks in connection with unitary tax issue (Article 9(4) of the Treaty), which was at that time a very important issue to the United Kingdom as it concerned a large number of major United Kingdom companies with investments in the United States. The brief of the United States in the Case has taken this sentence wholly out of the content. Moreover, my remarks were made in January 1977 prior to the publication of either the original or revised Technical Explanation which I am informed took place in March and July 1977, and clearly do not support the contention that the Technical Explanation was specifically part of the negotiated agreement with the United Kingdom, and, by inference, the proposition that the United Kingdom agreed to it.

12. Finally, I have been asked whether the United States Treasury interpretation of Article 23(1) is supported by and consistent with the policy underlying Articles 10 and 23 of the Treaty. In my opinion the United States interpretation is contrary to the policy which I understood underlay Articles 10(2)(a)(i) and 23(1)(c) of the Treaty. As I stated in comments delivered to the House of Commons in January 1977 (see column 1587 of my Exhibit 2) and again on 18th February 1980 (see columns 179 and 200 of my Exhibit 3), a fair balance had to be struck between United States and United Kingdom portfolio and direct investors. This was readily agreed to with regard to portfolio investors by a full and immediate refund by the United Kingdom subject to a 15 percent withholding tax. This gave the United States portfolio investor general parity with the United Kingdom investor because the United Kingdom gave the United

States investor an immediate net refund of 85 percent of the treaty credit and the United States gave an immediate section 901 credit of 15 percent of the treaty credit (under, so I am informed, Section 901 of the Code). Developing a fair balance for the United States direct investor was more difficult but was eventually accomplished by the United Kingdom giving an immediate 50 percent refund (subject to a 5 percent withholding tax which was currently creditable against United States tax liability) and the United States giving an indirect foreign tax credit for the other 50 percent under Article 23(1)(c). To strike the intended fair balance with United Kingdom shareholders, this indirect foreign tax credit had to be currently creditable. Therefore, to the extent that the United States Treasury Technical Explanation denies a current indirect foreign tax credit, it frustrates the policy underlying these provisions of the Treaty. Consequently, had the United States Government interpretation of Article 23(1) been brought to my attention as the responsible Minister of the United Kingdom Government, I would have raised objections to its interpretation of the Treaty as being in conflict with the policy underlying the Treaty.

13. I have not attempted in this affidavit to develop these matters in any detail, but if Judge Futey would find it helpful, I would be prepared to appear before the Court to address these matters.

[Signature]
Rees

[Notary Omitted in Printing]